

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

AMEREN ILLINOIS COMPANY)	
d/b/a Ameren Illinois)	
Petitioner)	Docket No. 12-0001
)	
Rate MAP-P Modernization Action Plan -)	
Pricing Filing)	

DIRECT TESTIMONY OF MICHAEL L. BROSCHE
ON BEHALF OF THE
PEOPLE OF THE STATE OF ILLINOIS
and AARP

DATED: APRIL 12, 2012

DIRECT TESTIMONY OF MICHAEL L. BROSCH

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EXHIBIT LIST

AG/AARP Exhibit No. 1.1 Summary of Qualifications

AG/AARP Exhibit No. 1.2 Prior Testimony Listing

AG/AARP Exhibit No. 1.3 AG Summary of Adjustments

AG/AARP Exhibit No. 1.4 Ameren's Response to RMP 1.01 (confidential)

AG/AARP Exhibit No. 1.5 Ameren's Response to AG 4.14, AG 1.07, AG 1.16,
AG 4.13 and AG 6.03

AG/AARP Exhibit No. 1.6 Ameren's Responses to AG 1.12, AG 4.05, AG 4.06
and AG 4.07.

AG/AARP Exhibit No. 1.7 Ameren's Responses to AG 4.01.

AG/AARP Exhibit No. 1.8 Ameren's Response to ST 2.07 (confidential) and ST 2.06 (confidential).

AG/AARP Exhibit No. 1.9 Ameren's Response to AG 4.16.

AG/AARP Exhibit No. 1.10 ComEd's Response to Staff DR DJK 1.10, ICC Docket No. 11-0721.

I. INTRODUCTION / SUMMARY

1 **Q. Please state your name and business address.**

2 A. My name is Michael L. Brosch. My business address is PO Box 481934, Kansas
3 City, Missouri 64148-1934.

4
5 **Q. By whom are you employed and in what capacity?**

6 A. I am a principal in the firm Utilitech, Inc., a consulting firm engaged primarily in
7 utility rate and regulation work. The firm's business and my responsibilities are
8 related to regulatory projects for utility regulation clients. These services include
9 rate case reviews, cost of service analyses, jurisdictional and class cost allocations,
10 financial studies, rate design analyses, utility reorganization analyses and focused
11 investigations related to utility operations and ratemaking issues.

12 **Q. On whose behalf are you appearing in this proceeding?**

13 A. I am appearing on behalf of the People of the State of Illinois represented by the
14 Attorney General, ("Attorney General" or "AG") and AARP.

15 **Q. Will you summarize your educational background and professional experience**
16 **in the field of utility regulation?**

17 A. Yes. AG/AARP Exhibit No. 1.1 is a summary of my education and professional
18 qualifications. I have testified before utility regulatory agencies in Arizona,
19 Arkansas, California, Florida, Hawaii, Illinois, Indiana, Iowa, Kansas, Michigan,
20 Missouri, New Mexico, Ohio, Oklahoma, Texas, Utah, Washington, and Wisconsin
21 in regulatory proceedings involving electric, gas, telephone, water, sewer, transit,
22 and steam utilities. A listing of my previous testimonies in utility regulatory
23 proceedings is set forth in AG/AARP Exhibit No. 1.2. In Illinois, I have testified in

several major proceedings before the Illinois Commerce Commission (“the Commission” or “the ICC”). These include Peoples Gas rate cases in Docket Nos. 90-0007 and 07-0241, North Shore Gas Company Docket No. 92-0242, Illinois Bell Telephone Company in Docket Nos. 92-0448 and 92-0239, ComEd rate case Docket Nos. 07-0566 and 10-0467 and Ameren Illinois Utilities Docket Nos. 07-0585 through 07-0590. I also testified in ComEd Docket No. 09-0263 involving the Advanced Metering Infrastructure Pilot Program and Associated Tariffs, in response to ComEd’s alternative regulation proposal that was filed in Docket No. 10-0527, and in the pending ComEd formula rate case, Docket No. 11-0721.

Q. What is the purpose of your testimony in this docket?

A. My testimony is responsive to the formula rate regulatory proposals and tariffs of Ameren Illinois Utilities (“Ameren”, “AIC” or “Company”) that are captioned as “Rate MAP-P Modernization Action Plan- Pricing Filing” (or “Rate MAP-P”). I will describe my understanding of formula rate regulation, as specified in new Section 16-108.5 of the Public Utilities Act (“PUA” or “the Act”), and then will discuss why certain of AIC’s specific proposals for implementation of formula rate regulation in this Docket are not reasonable and should be modified by the Commission in its Order. My testimony addresses the ratemaking concepts and procedures that are being recommended by AIC as well as specific rate case adjustments that are needed upon implementation of annual formula ratemaking.

Q. Please summarize the recommendations that are set forth in your testimony.

A. My testimony addresses several issues impacting the determination of Ameren’s asserted revenue requirement under the proposed formula rate and the subsequent “true-up” of such revenue requirements within annual reconciliation procedures that

are proposed in the testimony of Company witnesses Mill¹ and Stafford.² I explain the test year approach employed to develop the annual rate changes pursuant to formula and why it is essential that an average test year be used in the reconciliation procedures for determination of AIC's final revenue requirement in each future year. My testimony also addresses the interest rate that should be applied to over or under-recoveries of AIC's revenue requirement when reconciliation calculations are performed. The balance of my testimony then focuses upon and recommends specific ratemaking adjustments to ensure that future formula-based rates are just and reasonable.

With regard to Cash Working Capital ("CWC"), I recommend the conduct of additional studies to improve the accuracy of the estimated revenue collection lag and sponsor immediate revisions under AIC's flawed method now being used to estimate the revenue collection lag, so as to reduce the overstatement of CWC being proposed by the Company. I also propose utilization of AIC's calculated revenue lag associated with Pension expenses, which have been inexplicably ignored in the Company's lead lag study. I also revise Ameren's proposed lead/lag calculations that apply a revenue lag to pass-through tax and I correct Ameren's treatment of income tax expenses in calculating CWC.

I also propose several adjustments to test year operating revenues and expenses in my testimony. I recommend full, 100 percent revenue crediting of Late Payment (also known as Forfeited Discount) revenues in determining the Company's electric delivery service revenue requirement. The expense adjustments I sponsor include recognition of Commission approved amortization periods for

¹ Ameren Ex. 1.0.

certain regulatory assets, disallowance of certain lobbying, corporate branding, athletic event tickets and event sponsorship expenses, and removal of CWIP from rate base where AIC has no cash investment because project costs were financed by Accounts Payable.

Q. What information have you relied upon in formulating your recommendations?

A. I have relied upon AIC's pre-filed testimony and exhibits in this Docket, as well as the Company's responses to data requests submitted by Staff, the AG and other parties. I have also relied upon a copy of 220 ILCS 5/16-108.5 of the Public Utilities Act, which was provided to me by AG counsel. I also rely upon my prior experience with the regulation of public utilities over the past 31 years, including significant experience in Illinois and with alternative forms of regulation for telephone and energy utilities.

Q. Have you prepared any accounting schedules to summarize the adjustments being proposed in your testimony and by Mr. Effron?

A. Yes. AG/AARP Exhibit 1.3 is an eight page summary of the revenue requirement revisions being proposed by Mr. Effron and me. The first page of the Exhibit sets forth the Company's asserted formula revenue requirement from Ameren Exhibit 2.1. Adjustments are then posted in columns to the right of Ameren's asserted values, with supporting calculations appearing on subsequent pages, as referenced in the headings for each column. The sum of Mr. Effron's proposed adjustments is inserted at column (j) on page 1. It should be noted that Mr. Effron and I have not, with available time and resources, been able to conduct a complete review of all

² Ameren Ex. 2.0 through 2.2.

aspects of the Company's filing. As a result, the limited adjustments we are proposing should be viewed as cumulative with the work and recommendations of Commission Staff and other parties' witnesses.

Q. Ameren has proposed spreadsheet template forms for calculation of future rates and an extensive and detailed new Rate MAP-P for Commission review and approval in this Docket.³ Have you examined these documents in sufficient detail to propose all conforming adjustments that may be needed in connection with your ratemaking adjustments and proposals?

A. No. I have attempted to reference in my testimony the individual formula rate schedules where relevant calculations appear that would require modification upon Commission acceptance of my ratemaking proposals. However, I have not prepared a complete set of formula rate template revisions to address all of the issues that may be raised in these proceedings. I have also been unable with available time and resources to propose comprehensive edits to the 83 pages of proposed Rate MAP-P. Under these circumstances, I recommend that the Commission include in its order in this docket a requirement that Ameren submit conforming changes to Ameren Ex. 2.1 (formula template) and Ameren Ex. 9.1 (Rate MAP-P tariff) after the many issues raised in this proceeding have been resolved.

II. TEST YEAR PRINCIPLES AND USE OF AVERAGE RATE BASE IN THE RECONCILIATION.

³ Rate MAP-P appears at Ameren Exhibit 9.1.

117 **Q. What is the purpose of a “test year” in the determination of public utility**
118 **revenue requirements?**

119 A. Energy utilities have traditionally been regulated based upon their cost to provide
120 service, including an opportunity to earn a reasonable return on invested capital.
121 The process used to evaluate and measure the cost of service and resulting revenue
122 requirement is the rate case, in which a balanced review of jurisdictional expenses,
123 rate base investment, the cost of capital and revenues at present rates can be
124 undertaken at a common period in time, referred to as a “test year.” The proper
125 selection and consistent application of the test year is critically important, so that all
126 of the components of the revenue requirement, including rate base, operating
127 expenses, capital costs and sales or billing determinants are holistically analyzed
128 and quantified in a balanced and internally consistent manner with appropriate
129 “matching” of costs and revenues.

130 **Q. Are there several commonly employed types of rate case test years?**

131 A. Yes. The two broad categories of test years include “historical” test years that
132 employ actual recorded financial information to develop the revenue requirement
133 and “future” and “forecasted” test years that employ projections of expected future
134 financial information to develop the revenue requirement. Within these two broad
135 categories, the test year calculations can be based upon either an “average” set of
136 rate base and income data throughout the 12 months of the year or, alternatively, an
137 “end-of-period” or “annualized” approach that adjusts one or more elements of the
138 revenue requirement calculation to cost and revenue levels extant at year-end.

139 **Q. What type of test year has been proposed by Ameren in the determination of**
140 **its asserted first year formula rate-based revenue requirement?**

141 A. The Company's proposed test year is a hybrid, employing both historical and
142 forecasted information and both average and year-end information, as more fully
143 explained in the Direct Testimony of Mr. Stafford.⁴ The Company's proposed rate
144 base is measured as of December 31, 2010, and then is increased for projected plant
145 additions and for projected growth in Accumulated Depreciation through December
146 31, 2012.⁵ The Company has generally quantified the individual elements of rate
147 base as of test year-end, except for CWC that is quantified by lead/lag study and
148 Customer Deposits balances that are quantified as a 13-month average.⁶ Thus, for
149 rate base, Ameren proposes use of both historical and projected data and both
150 average and year-end quantification of specific rate base elements.

151 Ameren's test year operating income for ratemaking purposes is based
152 generally upon historical, average amounts as recorded in calendar 2010. Operating
153 expenses and depreciation/amortization expenses start at recorded calendar year
154 levels, with certain adjustments to account for cost recoveries through other tariff
155 mechanisms or to exclude costs not allowable for ratemaking purposes.⁷
156 Exceptions to this historical, average approach include projections of depreciation
157 expense associated with Ameren's projected plant in service additions and for
158 income tax expenses that are calculated applying statutory tax rates to a calculation
159 of ratemaking taxable income.⁸ Rather than calculating revenues at present rates for
160 comparison to the asserted revenue requirement, Ameren is proposing that its
161 overall test year revenue requirement be divided through annual billing

⁴ Ameren Ex. 2.0, pages 14-20.

⁵ Id. p.19.

⁶ Id. p. 15-19. See also Ameren Ex. 2.1, Schedule FR B-1 and referenced sources therein.

⁷ Ameren Ex. 2.0, p. 21-27; Ameren Ex. 2.1, Sch. FR C-1 and Sch. FR C-4.

⁸ Ameren Ex. 2.1, Sch. FR C-2, line 10 and Sch. FR C-4, lines 1-5.

determinants, so as to set revised tariff prices and the billing determinants that are based upon average 2010 billing determinants, including weather normalized sales volumes.⁹

Q. Will the revenue requirement and new rates resulting from Ameren’s initial installment of annual formula rate changes later be subjected to reconciliation and “true-up” provisions under Section 16-108.5?

A. Yes. Each May 1, Ameren proposes to file its calculation of prospective changes to the formula rate revenue requirement using inputs from the prior year’s FERC Form 1 and other data sources. As part of this filing, Ameren would then also calculate a reconciliation to “true-up” the previously approved revenue requirement, which had incorporated projections of changes in plant investment, accumulated depreciation and depreciation expense, to determine a revised revenue requirement for the same period using then available actual recorded data.¹⁰

Q. Has Ameren proposed any particular test year approach for calculation of the reconciliation revenue requirement?

A. There is no discussion of reconciliation test year concepts in the Company’s prepared testimony, but the references appearing in Ameren Ex. 2.1 at Schedule FR A-1-REC indicate the Company’s intent to again use a year-end rate base to calculate the reconciliation revenue requirement so as to “true-up” previously approved revenue levels.¹¹

⁹ Ameren Ex. 9.0, p.3-4; Ameren Ex. 9.1, p.1-3.

¹⁰ Ameren Ex. 1.0, page 26.

¹¹ Ameren Ex. 2.1, Schedule FR A-1-REC at line 11 indicates an intended “Source” for the “Rate Base-Reconciliation” value would be Schedule FR B-1 at line 36, which amount is the sum of recorded year-end DS Rate Base balances, prior to projected Plant additions for the subsequent year.

182 **Q. Is it appropriate to employ a year-end rate base in calculating the**
183 **reconciliation revenue requirement that would “true-up” costs using actual**
184 **information?**

185 A. No. The reconciliation calculation should employ an average rate base to properly
186 quantify the return on investment elements of the revenue requirement. The proper
187 level of return for investors should reasonably compensate the actual level of capital
188 invested in the delivery service business throughout the true-up period. Adoption of
189 Ameren’s proposed reconciliation approach, that would apply the allowed rate of
190 return to year-end rate base, would systematically overstate the true-up rate base and
191 resulting reconciliation revenue requirement. AIC’s investment in assets serving
192 delivery service customers is generally higher at year-end than throughout the
193 reconciliation year.

194 **Q. Does Ameren’s decision to be a “Participating Utility” under Section 16-108.5,**
195 **as stated in the Company’s Verified Petition,¹² cause the decision regarding use**
196 **of an average versus year-end rate base in the reconciliation to be an important**
197 **issue?**

198 A. Yes. The Company is committing to making incremental investments in electric
199 system upgrades estimated at \$625 million over ten years, with \$265 million for the
200 purpose of electric system upgrades and \$360 million for smart grid deployment.¹³
201 These “incremental” investments totaling \$625 million are above and beyond
202 Ameren’s normal pace of spending to accommodate replacement of aging plant,
203 customer growth and other ongoing capital programs. If we assume ratable capital
204 spending and the impact of only the incremental investment commitments in years

¹² Verified Petition, page 2, paragraph 3.

one through ten of the program, annual rate base growth caused by the new investments could average about \$62 million per year.¹⁴ The “value” of reconciling the revenue requirement using year-end versus average rate base would be approximately one-half the ratable investment growth expected each year, since the mid-point of spending in a typical future year could be at the \$31 million level of plant additions, while by year-end plant additions could total the \$62 million.¹⁵ Translating this typical rate base difference of \$31 million into revenue requirement would produce additional annual revenues for AIC after reconciliation of approximately \$4.4 million per year.¹⁶

Q. Does Ameren, in fact, anticipate significant and continuous growth in its ratemaking capital structure in every year of the infrastructure investment plan for which it has prepared projections?

A. Yes. The Company’s confidential response to Staff Data Request No. RMP 1.01 in Attachment 2 provided projections showing substantial year over year growth in both the Company’s total Capitalization and in its Net Property Plant and Equipment assets that comprise the majority of the rate base each year. With persistently growing future rate base investment levels, there is no doubt that using a year-end rate base in the reconciliation of annual revenue requirements will overstate charges to customers and inflate the Company’s return on actual investment, relative to the actual cost of capital for the year being examined. I have

¹³ Id.

¹⁴ \$625 million / ten years.

¹⁵ This simplified example ignores changes in other elements of rate base, arising from ongoing capital spending on non-incremental programs, continued growth in Accumulated Depreciation, and changes in Accumulated Deferred Income Taxes and other elements of rate base which are assumed to be largely offsetting in this discussion.

included a copy of this confidential response as AG/AARP Exhibit 1.4

(Confidential).

Q. Can you provide an illustration of how the Company's proposed use of a year-end rate base will inflate the Company's return on actual investment?

A. Yes. To illustrate the problem, we can assume steady annual growth in future rate base and the corresponding amount of common equity capital in the utility, at a pace of five percent per year spread evenly throughout each year. The following table shows the impact upon equity returns of targeting an assumed nine percent ROR on such a growing rate base, but then calculating revenue requirements on year-end, rather than average invested capital:

Illustration of Average VS Year-end Rate Base (\$ millions) - post tax return and ROE % difference

Year	<u>Projected Rate Base</u>			<u>Return at 9% on Rate Base</u>		Return Difference	Average Equity @ 54%	ROE Impact
	Beg. Of Year	End of Year	Average	End of Year	Average			
1	2,000	2,100	2,050	189	185	5	1,107	0.41%
2	2,100	2,205	2,153	198	194	5	1,162	0.41%
3	2,205	2,315	2,260	208	203	5	1,220	0.41%
4	2,315	2,431	2,373	219	214	5	1,281	0.41%
5	2,431	2,553	2,492	230	224	5	1,346	0.41%

With these assumptions, the post-tax return available for return on equity ("ROE") capital exceeds the intended ROE by approximately 41 basis points each year, adding about \$5 million of return costs, plus the related factor-up for income taxes, to the revenue requirement burden faced by ratepayers. If rate base grows more rapidly than five percent per year, the ROE variance relative to intended earnings levels would be even larger, and vice-versa.

¹⁶ Based upon Ameren's asserted pretax overall return rate of %, derived from Ameren Ex. 2.1 as the sum of "Authorized Return" of \$195,559 plus "Incremental Tax Gross-up" of \$109,174 = \$304,773, then divided by "Rate Base" of \$2,168,258 = 14.05%.

242 **Q. Why does the use of a year-end rate base force the achieved ROE to be higher**
243 **than the intended ROE?**

244 A. The utility's actual investment in new plant and the corresponding growth in newly
245 invested equity and debt capital tend to grow gradually throughout the year.
246 Therefore, the associated return requirement for such capital also grows gradually
247 throughout the year. If the revenue requirement calculation is improperly based
248 upon the year-end level of such rate base investment, as if that investment were
249 fully incurred on January 1 and existed in all months of the test year, the resulting
250 return requirement is systematically overstated. This is the financial result caused
251 by Ameren's proposal to utilize a year-end rate base within the reconciliation
252 process.

253 **Q. If return requirements are overstated, relative to the actual amounts of capital**
254 **being invested only gradually throughout a test year, why would regulators**
255 **ever allow utilization of a year-end rate base?**

256 A. The only valid reason for employing a year-end rate base in an otherwise average
257 test year approach is to reduce regulatory lag by approximately six months, which is
258 the difference between the mid-point of an historical test year and year-end. It
259 should be noted that when a year-end or "annualized" rate base is used by
260 regulators, it is common for other elements of the revenue requirement such as
261 wage rates, employee headcounts, customer counts, depreciation expense and other
262 known changes to be similarly annualized at year-end. The combined impact of
263 such broadly applied annualization adjustments is to reduce regulatory lag.

264 **Q. If AIC’s revenue requirements are to now be annually trued-up, so as to fully**
265 **recover jurisdictional actual incurred costs, is there any remaining need to**
266 **address regulatory lag through use of a year-end rate base?**

267 A. No. Traditional test-year regulation involves setting utility rates that remain
268 unchanged until the “next” rate case is filed, causing regulatory lag to exist when
269 cost changes occur between test year rate cases. However, regulatory lag concerns
270 are completely mitigated by the new formula ratemaking regime, where Ameren
271 will be made “whole” with interest for changes in all of its actual jurisdictional
272 costs incurred to provide delivery services in Illinois. When the formula-based
273 revenue requirements, which are inclusive of projected net plant in service
274 additions, are trued-up through the reconciliation process to actual cost levels, any
275 revenue requirement variances are allowed interest charges to be sure that
276 regulatory lag imposes no financial consequences on AIC. In this new regulatory
277 environment, there is absolutely no need for the Commission to permit the use of
278 year-end rate base as a remedy for regulatory lag.

279 **Q. With the new annual reconciliation process in place to true-up Ameren’s**
280 **asserted revenue requirement to its actual cost levels, does it matter whether**
281 **the revenue requirement at the inception of formula ratemaking utilizes a**
282 **year-end versus an average rate base?**

283 A. Not particularly. The methodology being used to develop the inception revenue
284 requirement, such as depicted on Ameren Ex. 2.1 at Schedule FR A-1, is of less
285 importance to AIC’s earnings than the method to be used in the future when
286 calculating the true-up charges or credits to customers in future reconciliation

proceedings.¹⁷ The revenue requirement that is ultimately payable by ratepayers is the amount calculated after reconciliation, plus any associated carrying charges on such over or under-recoveries. The Commission's goal should be to adopt a revenue requirement calculation method that yields a reasonable approximation of the ultimate revenue requirement owed AIC upon reconciliation so as to minimize the size of future reconciliation revenue adjustments.

Q. In Ameren Ex. 2.1, the Company has proposed a spreadsheet template to document the calculation steps to be employed in administering Rate MAP-P. What changes to this template are needed to ensure that the reconciliation of revenue requirements is performed using an average rate base approach?

A. The simplest revision would be to insert two additional lines at what is presently identified as Sch. FR A-1-REC in the proposed spreadsheet template. The existing line 11 of this Schedule now references Sch. FR B-1 at line 36 to insert a year-end rate base from the current filing made each year. I would insert one additional line beneath existing line 11 to insert from the prior year's filing the Sch. FR B-1, line 36 recorded year-end rate base at December 31 of the previous year. Then a second new line would be inserted to calculate the mathematical average of the prior year-end and current year-end rate base values to quantify an average rate base for purposes of calculating the "Net Revenue Requirement – Reconciliation" on Schedule FR A-1-REC each year.¹⁸ Conforming changes would be needed within

¹⁷ This is not to say that inception rates are unimportant to ratepayers or the utility, where actual monthly bills payable by consumers are directly impacted by inception rate levels and the Company's cash flows are also impacted by the level of inception rates.

¹⁸ It should be noted that Ameren Ex. 2.1 at Sch. FR A-3, at line 1, employs a "DS Rate Base" value from Sch. FR B-1 line 36 for determination of the ROE Collar Computation. The changes proposed herein for derivation of the DS Rate Base on an average basis within Sch. FR A-1-REC should also flow through to the ROE Collar computation.

the Rate MAP-P to effect reconciliation of the revenue requirement on an average rate base approach.

A more complex calculation of the actual average rate base used in reconciliation could be employed, that would require more elaborate spreadsheet template revisions than are recommended above. For example, certain elements of the rate base that are included in the amounts used above are not presently quantified at a single point in time, but are instead based upon 13-month averages or specific calculations, such as customer deposits and CWC. It may be worthwhile in the interest of accuracy to substitute the most currently available 13 month averages or separately calculated CWC amounts within the average rate base amounts being used in reconciliation. These more complex calculations could be ordered by the Commission to be included in a compliance filing from AIC once the more substantive issues involving the reconciliation process are resolved.

Q. Are you responsible for development and presentation of the rate base to be used in calculating the initial formula rate case revenue requirement in this Docket?

A. No. AG witness Mr. Effron is addressing the rate base issues on behalf of the Attorney General and AARP, except for Cash Working Capital and the CWIP adjustments, which are discussed later in this testimony.

III. RECONCILIATION INTEREST CHARGES.

Q. Please describe the Company's proposal with regard to the application of interest charges to the revenue requirement reconciliation balance.

330 A. Ameren proposes to apply a “Monthly Interest Rate” of 0.752% to the revenue
331 requirement “Variance – Reconciliation Before Interest” amount calculated on
332 Ameren Ex. 2.1 at Sch. FR A-4, lines 1 through 3. This percentage represents 1/12
333 of the calculated Weighted Average Cost of Capital that is calculated at Sch. FR D-
334 1 and appears at line 23. Thus, AIC is proposing that the revenue requirement
335 difference arising from the reconciliation process, whether positive or negative, be
336 allowed to earn the Company’s calculated overall cost of capital, rather than simple
337 interest as provided for in the Act.

338 **Q. Does new Section 16-108.5 of the Act specify the interest rate to be applied to**
339 **the revenue requirement reconciliation balances until such amounts are**
340 **charged or credited to ratepayers?**

341 A. No. Section 108.5(d)(1) of the Act states, “Any over-collection or under-collection
342 indicated by such reconciliation shall be reflected as a credit against, or recovered as
343 an additional charge to, respectively, with interest, the charges for the applicable
344 rate year.” However, it does not specify the appropriate interest rate to be used for
345 this purpose.

346 **Q. Should the revenue requirement variances calculated for reconciliation**
347 **purposes be allowed interest at Ameren’s overall cost of capital?**

348 A. No. The amounts in question represent short term assets or liabilities that are to be
349 either charged or credited to ratepayers within the annual rate adjustment
350 mechanism. These balances therefore do not require permanent financing by
351 Ameren, and should not be expected to require new Ameren common stock
352 issuances or parent company equity infusions for financing. There is no basis to
353 assume that incremental equity financing will occur in connection with the annual

revenue reconciliations. Therefore, AIC's proposed interest rate that is based upon its overall cost of capital, including a weighted equity return element, should be rejected.

Q. What would be a more appropriate rate of interest for application within AIC's proposed formula rate template spreadsheet, at Ameren Ex. 2.1, Schedule FR A-4, line 4, in the Reconciliation Computation?

A. A short term debt interest rate should be used for this purpose, recognizing Ameren's ability to access credit markets at favorable cost rates to finance short term asset investments. For example, the average cost of short term debt to Ameren Corporation was only 2.3% in 2011.¹⁹ An alternative cost rate for consideration is the interest rate Ameren currently pays on customer deposit balances, which is presently zero percent.²⁰

Q. Would utilization of a short term debt cost rate to calculate interest to be applied to revenue requirement reconciliation balances be beneficial to AIC ratepayers?

A. Yes. Short term debt cost rates have recently remained at historically low levels and tend to be generally lower than the costs of more permanent debt capital most of the time. With the large anticipated infrastructure investments AIC will make pursuant to new Section 16-108.5 and because inflation impacts upon annual operating expenses are not projected beyond test year end in setting formula rates, it is reasonable to expect future reconciliations to often yield balances chargeable to

¹⁹ The Ameren Corporation SEC Form 10-K for fiscal year ended December 31, 2011 at page 113 summarizes Ameren parent and Genco borrowings under the Credit Agreements that provide short term debt and liquidity to the corporation. The weighted average interest rate paid on outstanding borrowings in 2011 was 2.30%.

²⁰ Rate determined by the Commission in Docket No. 11-0793, approved December 21, 2011.

ratepayers. Under these circumstances, a relatively lower interest rate would be beneficial to ratepayers.²¹

Q. Is there another accounting measure that could appropriately be employed to determine the interest cost applicable to revenue requirement reconciliation variances?

A. Yes. The Commission could deem the revenue requirement variances under formula ratemaking to be regulatory assets that represent a deferral of operating expenses to be recoverable (or returnable) in future rate periods. Since operating expenses are income tax deductible when incurred by the taxpayer, the deferred income tax balances associated with such expense deferrals could be used to reduce the balance upon which interest is accrued. Application of interest to only the net of income tax balance associated with such deferrals is consistent with the economic reality that income tax savings would be realized from AIC's delayed recovery of tax deductible expenses and would serve to reduce the overall interest burden upon ratepayers by about 40 percent.

Q. Would it be reasonable to deem the revenue requirement reconciliation balances to be deferred operating expenses for this purpose?

A. Yes. The formula-based revenue requirement subject to later reconciliation includes the forecasted amount of all jurisdictional additions to net plant in service within rate base, but does not provide for projections of inflation in the utility's operating expenses. Aside from differences between actual and forecasted net plant in service amounts, the majority of the revenue requirement upon true-up to actual costs is

²¹ In AG 6.06, AIC was asked if "the Company anticipates the future reconciliation adjustments that will be experienced under formula ratemaking will tend to be under-recovery amounts to be

likely to be caused by changes in operating expenses where no cost inflation projections are included.

Q. What changes to Ameren Ex. 2.1, Sch. FR A-4, the formula rate spreadsheet template “Reconciliation Computation,” are required in order to apply your recommendations?

A. First, the “Variance” appearing at line 3 should be reduced by associated incremental deferred income taxes using the Company’s composite Effective Income Tax Rate, which is derived on Sch. FR C-4, at line 4. The calculation and subtraction of related Accumulated Deferred Income Taxes could be inserted as new lines 4 and 5 on Sch. FR A-4. Then, the “Monthly Interest Rate” on line 4 (to be renumbered line 6) should be modified to tie to Ameren’s current cost of short term debt, to be determined within App 12 of the template.

IV. CASH WORKING CAPITAL ISSUES.

Q. Has the Company proposed an allowance for Cash Working Capital (“CWC”) within the rate base used to establish annual formula rates?

A. Yes. Ameren Ex. 2.1 at App 3 is the Company’s proposed calculation supporting an allowance for CWC of \$11,631,000 that is sponsored by witness Mr. Heintz in Ameren Ex. 4.0. The same calculations for CWC appear in Mr. Heintz’ Ameren Ex. 4.2 and at Ameren Ex. 2.2, page 69 which is captioned Workpaper 3.

Q. Was a lead lag study adopted by the Commission to determine CWC in the most recently completed AIC rate cases?

420 A. Yes. However, considerable controversy surrounded the lead lag study proposed by
421 AIC in Docket Nos. 09-0306 through 09-0311, consolidated. In the Commission's
422 Order dated April 29, 2010, the Companies' asserted revenue collection lag was
423 rejected by the Commission, with the following explanation:

424 The Commission has concerns about AIU's proposed method for
425 calculating the CWC requirement. The Commission understands
426 that IIEC's reason for proposing 21 lag days is that it is the
427 maximum lawful period customers can delay payment. Section
428 285.2070 of Part 285 specifically contemplates the use of a lead/lag
429 study. AIU presented a detailed lead/lag study using methods that
430 have been adopted by the Commission in numerous previous
431 proceedings, but AIU assumed, rather than proved, the collection
432 lag periods used in its study. The absence of empirical evidence
433 supporting the collection lag assumptions used in Ameren's lead/lag
434 study weighs against the utility, which has the burden of proof in
435 this proceeding. Under these circumstances, IIEC's proposal to use a
436 21 day collection lag in calculating the CWC requirement is hereby
437 adopted. [Final Order page 54]

438

439 An additional disputed issue involved the lead lag study treatment of pass-through
440 taxes. The Commission adopted the Staff's adjustment to the Companies' CWC
441 proposal, stating:

442 As an initial matter, the Commission accepts Staff's
443 argument that the utility has no "investment" associated with pass-
444 through taxes. Since every dollar for pass-through taxes is collected
445 from the ratepayers, the inflows and outflows earmarked for these
446 taxes should be perfectly balanced. Thus the need for CWC should
447 not arise with respect to pass-through tax transactions. This
448 conclusion is consistent with prior Commission decisions. Nicor
449 Docket No. 08-0363 at 11-12.

450 Staff distinguishes pass-through taxes from other cash flows in that,
451 unlike other revenue, pass-through taxes are not directly associated
452 with the provision of utility service. The Commission believes that
453 Staff makes a legitimate point here. The Company would have us
454 believe there is an additional and measurable cost to pass-through

taxes but fails to illustrate how a tax that is completely ratepayer-funded could generate any costs or expense. This is simply not the case. The Commission finds that Staff's proposed adjustment to the CWC requirement must be accepted. [Id.]

In its Order on Rehearing issued November 4, 2010, the Commission revised its decision regarding the revenue collection lag day after concerns were raised by AIU regarding the inclusion of significant amounts of late fee revenues while the ICC-approved revenue collection lag assumed customers' remittances fell generally within the Commission's 21-day payment rules:

While the evidence and arguments on Rehearing are not what the Commission anticipated, they are helpful in considering the issue of CWC and the Commission appreciates the input of the parties. It appears that no party disputes AIU's estimate of the revenue it receives in late payment fees. While IIEC disputes that AIU incurs a cost associated with late payments, it does not appear to contest the method for quantification offered by AIU. The Commission's review of the record indicates that AIU actually has collected revenues associated with late payments. The fact that AIU collects late fees suggests that some customers pay their bills after the dates specified in the Commission's rules. If all customers paid their bills by the time specified in the Commission rules, it would not be possible for AIU to collect late fees.

IIEC argues there is no connection between the amount of late fees collected and AIU's estimate of the capital costs associated with late payments. The Commission believes, however, that inherently, if a customer does not pay its bill in a timely manner, it will be necessary for a utility to finance its operations in interim with an alternate source of capital. This is the entire reason for a CWC allowance and a lead/lag study.

The Commission is of the opinion that the methodology espoused by AIU and Staff is the most appropriate for calculating AIU's CWC allowance in this instance. The position of AIU, as adopted by Staff, persuasively shows the effect of the late fee revenue on AIU's capital costs, and as such it will be adopted by the Commission on Rehearing. [Order on Rehearing, p.56]

This historical perspective regarding lead lag study issues is important, because in its formula rate calculations, AIC is again employing the same form of revenue collection lag calculations used in Docket Nos. 09-0306 through 09-0311, under which the Company has assumed, rather than proven, dates when customers, on average, actually remit payments of their utility bills.

Q. In your Direct and Rebuttal Testimony in ComEd’s last rate case, Docket No. 10-0467, and in ComEd’s pending formula rate proceeding, Docket No. 11-0721, you explained a number of problems with that utility’s method of calculation to estimate the revenue collection lag. What is the nature of that problem?

A. The problems I noted in the ComEd case are similar to the problems addressed by the Commission in Ameren Docket Nos. 09-0306 consolidated. ComEd, Ameren and other Illinois utilities have adopted a shortcut method to estimate the revenue collection lag, in place of more traditionally used methods that more accurately quantify this important lead lag study value. This shortcut method was characterized in the previously quoted Commission Order as, “...AIU assumed, rather than proved, the collection lag periods used in its study. The absence of empirical evidence supporting the collection lag assumptions used in Ameren’s lead/lag study weighs against the utility, which has the burden of proof in this proceeding.” The revenue lag is the single most important lag value in a study of CWC, because it is applied to the largest amount of dollars, i.e., the entire revenue stream of the utility. For this reason, shortcut estimation of the revenue collection segment of the overall revenue lag is inappropriate.

515 Since lead lag studies first emerged in the 1980s as the preferred and most
516 accurate approach to quantify CWC, measurement of the revenue collection lag has
517 most frequently been quantified using either a statistical sampling of actual
518 customer remittances or a calculation of daily average Accounts Receivable
519 “turnover” ratios that indicate the average number of days of revenues outstanding
520 calculation. The Commission’s recent, repeated acceptance of the utilities’
521 unsubstantiated assumptions about when customer payments are received is an
522 arbitrary methodology not commonly used in the states in which I have testified.
523 Either of the alternative, more precise methods I reference above can produce
524 reasonable estimates of how quickly utility customers actually pay their bills and
525 have received widespread acceptance among regulators. However, either as a result
526 of limited data availability and/or an interest in overstating revenue collection lags,
527 the Illinois utilities I mentioned have achieved some success convincing this
528 commission that arbitrary mid-point remittance assumptions applied to broad
529 categories of aged receivables can achieve a reasonable result. Unfortunately, this
530 is not the case and action should be taken by Ameren to improve upon the accuracy
531 of revenue collection lag quantification. I strongly urge the Commission to revisit
532 this issue in this case in order to ensure that AIC’s are not paying excessive rates.

533 **Q. Does the Ameren lead lag study in the instant Docket incorporate the same**
534 **flawed receivables aging mid-point methods?**

535 **A.** Yes. The revenue collection lag underlying AIC’s asserted CWC amounts is being
536 estimated by Mr. Heintz through application of very crude assumptions to quite
537 broad “aged” categories of month-end accounts receivable balances. Mr. Heintz
538 has not actually measured how long it takes to collect revenues from Ameren

customers. Instead he looks to a breakdown of the Companies' recorded week-end Accounts Receivable balances by customer class and assigns, without any supporting analysis, the following arbitrarily assumed revenue collection dates to each grouping of aged receivable balances:

Receivable Age>>	0 – 30 Days	31 - 60 Days	61 – 90 Days	Over 90 Days
Residential	15	45	75	90
Non-Residential	15	45	75	90

For example, every one of the thousands of residential customer accounts with balances ages that ranged from 0 to 30 days old were arbitrarily assumed to be remitted precisely on day 15; while accounts ranging from 31 to 60 days old were assumed to be remitted precisely at the mid-point of this period, on day 45, and all residential customer accounts with balances 61 to 90 days old are assumed to be fully paid to AIC precisely on day 75, which is again the mathematical mid-point of the period. For all customer account balances more than 90 days old, a statistically impossible average age of 90 days was assumed by Mr. Heintz in place of an alternative mid-point assumption.

Q. In Docket Nos. 10-0467 and 11-0721, did ComEd attempt to limit the financial impact of some of the gross inaccuracies arising from the utilization of arbitrary Accounts Receivable aging mid-point assumptions?

A. Yes. ComEd applied certain “grace period” assumptions to the youngest aging categories in an effort to introduce conservatism into the otherwise unsupportable mid-point assumptions that were applied to aged accounts receivables. For example, because residential customers have 20 days before their unpaid utility bills

are delinquent, ComEd assigned an assumed zero lag value to all residential balances 0-30 days old. ComEd also assigned an 8-day assumed remittance date to its small and large commercial accounts falling within the same aging category because of payment due date terms in the Commission's rules. These changes did not remedy the inherent inaccuracy caused by using unproven mid-point assumptions applied to each Accounts Receivable aging category, but they did produce a result for ComEd that was somewhat more credible than could be calculated without injecting these additional assumptions regarding grace periods.

Q. How did ComEd's witness describe the grace period assumptions in Docket No. 11-0721?

A. ComEd's lead lag study was sponsored by Mr. John Hengtgen.²² In his Direct Testimony for ComEd, Mr. Hengtgen explained the multiple adjustments he made to accounts receivables aging mid-point assumptions as follows:

In several areas, I made calculations in which the result reflected a conservative cash working capital requirement. For the collection lag calculation, I excluded accounts receivable amounts over 365 days old and I also excluded amounts related to inactive accounts. In calculating the collection lag, I also did not incorporate lags for the various grace periods that the different classes of customers have to pay their bills, resulting in a conservative calculation.

These more conservative assumptions, if applied by Mr. Heintz within the AIU lead lag study, would produce significantly different CWC results. However, Mr. Heintz has completely ignored the payment due date grace periods that customers have to pay their bills. Additionally, the Ameren study does not exclude accounts

²² ComEd Ex. 9.0.
Docket No. 12-0001

receivable amounts over 365 days old or the amounts related to inactive accounts.

These are additional reasons why the AIU asserted CWC value is overstated.

Q. What is your recommendation regarding the amount of CWC that should be included in Ameren's rate base at this time?

A. I recommend at this time, and only for initial determination of the inception rates that will later be subject to reconciliation, that the Company's proposed lead lag study at Ameren Ex. 2.1, App 3 and Ex. 4.2 be modified to reflect the following changes and then employed to set rates:

1. Revision of Ameren's estimated revenue collection lag to insert reasonable grace period assumptions, as were used in ComEd's calculations approved by the Commission in Docket No. 10-0467, so as to provide conservatism and recognition of the period within which residential and commercial customers' bills are payable but not delinquent.
2. Reinstatement of the Commission's ordered treatment of pass-through taxes, assigning no revenue lag to these amounts where Ameren serves as the collection agent and not tax is owed until after revenues are collected by Ameren.
3. Inclusion of cash flow payment lag days for pension expense funding within the employee benefits lag included in determining CWC.

I further recommend that, before any CWC allowance is permitted in future formula rate changes or as part of the reconciliation of 2012 revenue requirements to actual costs in the Company's May 2013 filing, AIC be ordered to conduct a more

extensive analysis of its actual revenue collection lag days and revise the CWC calculations to reflect the results of such study, as more fully described herein.

Q. Have you prepared an Exhibit to summarize the changes you are recommending to Ameren's CWC calculations?

A. Yes. AG/AARP Exhibit 1.3 at page 2 is a spreadsheet calculation that reformats and summarizes Ameren's lead/lag study Ex. 2.1, App.3, to show the line by line impact of each cost element included in the Company's lead/lag study. Lines 1 through 17 and columns (a) through (g) of my Exhibit replicate the Company's results on Ameren Ex. 2.1 App. 3, but combine the Revenue Lag and Expense Lead for each line items so as to show the overall CWC impact of each element of the analysis. This presentation format is useful in isolating the CWC effects associated with the lead/lag study treatment of each category of transaction.

After this restatement of the Company's study, I present at columns (h) through (l), a side-by-side calculation showing each change I am proposing to illustrate the resulting differences in CWC. The cells in columns (h) and (i) are shaded where an AG change to study inputs has been made.

Q. Please describe the elements within Ameren's asserted 49.75 Revenue Lag Days, as shown in column (c) of AG/AARP Exhibit 1.3.

A. Ameren's revenue lag is comprised of five segments, including:

1. A customer usage or service period lag of 15.21 days, plus
2. An average billing period lag of 1.51 days, plus
3. A collection lag between the billing date and customer remittances estimated at 30.67 days by Ameren, plus

631 4. A payment processing lag of 1.39 days for processing and depositing of
632 remittances, plus

633 5. A bank float of 0.97 days until deposited funds are available for use by
634 AIC.²³

635 As noted previously in my testimony and in the Commission's previous rate order,
636 there are major problems with the third element of the Company's calculation that
637 must be corrected. Ameren should be required to undertake a systematic study of
638 the timing of customers' actual remittances to more accurately estimate its revenue
639 collection lag; using either of the two generally accepted methods used in other
640 regulatory jurisdictions that employ lead lag studies. Until improvements are made
641 in this area, the Company's lead/lag study is hopelessly inaccurate and should not
642 be relied upon in any future formula ratemaking process.

643 **Q. Why are your revised Revenue Lag Day values that shown in column (h) of**
644 **AG/AARP Exhibit 1.3, page 2, so much lower than Ameren's 49.75 day overall**
645 **revenue lag that is set forth in column (c)?**

646 A. I have revised the Company's revenue collection lag calculations to insert the same
647 grace period customer remittance assumptions that were previously adopted by
648 ComEd and that were approved by the Commission in Docket No. 10-0467. These
649 assumptions serve to replace Mr. Heintz's assumed 15-day collection lag
650 assumption for the 0-30 day aging category with an assumed zero and eight lag day
651 value, for residential and commercial receivables, respectively. I have retained all
652 of the Company's other arbitrary assumptions and methods in estimating the
653 revenue collection lag calculations, that are used to determine my revised overall
654 revenue lag in column (h) of 41.12 days.

²³ Ameren Ex. 4.0, Page 8.

655 **Q. How specifically did ComEd consider payment due date grace periods when**
656 **estimating the revenue collection lag?**

657 A. For residential service the due date on the bill cannot be less than 21 days after the
658 delivery date on the bill, and for non-residential service, the due date cannot be less
659 than 14 days. No late payments charges can be assessed until utility service
660 becomes past due under these limitations.²⁴ These due date grace periods that are
661 specified in the Commission's rules should be considered in formulation of the
662 assumptions applied to aged receivables, if the flawed accounts receivable aging
663 methodology is employed at all. Since these grace period assumptions were found
664 reasonable for ComEd, there is no reason to apply different assumptions in AIC's
665 lead lag study calculations. I have included a copy of ComEd's response to Staff
666 Data Request DGK 1.10 from ICC Docket No. 11-0271 as AG/AARP Exhibit No.
667 1.10 to explain how grace periods were considered in the lead lag study approved
668 by the Commission in Docket No. 10-0467 and similarly used by ComEd in
669 pending Docket No. 11-0721.

670 **Q. How significant is the CWC impact of revising Ameren's collection lag and**
671 **overall revenue lag for the effects of billing grace periods, using ComEd's**
672 **methodology?**

673 A. The collection lag component of the revenue lag changes from 30.67 days in AIC's
674 study to 22.04 days using the ComEd grace period assumptions. This 8.63
675 reduction in collection lag days results in a revised overall revenue lag of 41.12
676 days, compared to Ameren's proposed 49.75 day revenue lag. The overall impact

677 upon CWC included in rate base from a 8.63 day reduction in the revenue lag is
678 approximately \$13.2 million less Cash Working Capital in rate base.²⁵

679 **Q. After your proposed adjustment to account for payment due date grace**
680 **periods, is the Company’s revenue collection lag estimate reasonable for future**
681 **use by the Commission?**

682 A. No. The revised revenue lag day value resulting from the inclusion of grace period
683 assumptions will significantly improve the reasonableness of the Company’s study,
684 by injecting conservatism into the results produced by Ameren’s inherently
685 imprecise and arbitrary mid-point assumptions, with no actual measurement of
686 customer remittance timing. However, an actual measurement of the revenue
687 collection lag should be required of AIC in the future.

688 **Q. What specifically should be required of AIU in the future to correct its**
689 **estimated revenue collection lag day value?**

690 A. The Company should be required to conduct statistical samples of actual customer
691 remittances, to determine the average number of days between collection date and
692 the related prior billing date(s). Alternatively, the Company should be required to
693 collect and analyze its average daily electric service accounts receivables balance,
694 net of the related uncollectibles reserve, to quantify how many days of its sales are
695 “outstanding” within these balances. This Accounts Receivables “turnover”
696 calculation relies upon dividing the net average daily balance of Accounts
697 Receivables by annual utility sales revenues and is routinely used in other

²⁴ 83 IAC 280.90. For governmental customers and school districts, this grace period is expanded to 45 days after the bill is rendered.

jurisdictions to quantify the revenue collection lag for energy utilities. I recommend that Ameren be required to employ either or both of these methods in future lead lag studies to actually measure customer remittance patterns and more accurately quantify the revenue collection lag, before any future CWC amounts are included in rate base.

Q. Why is the lag day value for Employee Benefits you proposed at line 1 of AG/AARP Exhibit 1.3, page 2 in column (i) different than the Company's proposed Employee Benefits lag day value in column (e)?

A. Mr. Heintz' workpapers include calculations of payment dates and amounts for each element of employee benefits, including Medical and Dental plan payments, life insurance funding, 401k funding and pension plan funding. However, in compiling the overall Employee Benefits lag day value, the Company did not include the calculated payment lag data for pensions. So as to more completely account for cash flow patterns associated with Employee Benefits, I have accepted and included the Company's calculations capturing the timing of pension funding payments within the test year Employee Benefits lag day value. Ameren has provided no justification for ignoring this significant employee benefit cash payment in calculating the lag day value assigned to Employee Benefits.

Q. At lines 10 through 12 of AG/AARP Exhibit 1.3, page 2, you have set to zero the revenue lag days associated with pass-through charges for Energy Assistance Charges, Municipal Utility taxes and Gross Receipts Taxes. Why is this necessary?

720 A. As noted in the quotation at lines 442 to 458 above, in Docket Nos. 09-0306
721 through 09-0311 consolidated, the Commission found in favor of Staff's position
722 that pass through taxes are completely ratepayer funded and have no CWC impact
723 because the inflows and outflows earmarked for these taxes occur after taxable
724 revenues have been collected by the utility. Thus the need for CWC should not arise
725 with respect to pass-through tax transactions. Again in ComEd Docket No. 10-
726 0467, the Commission found that pass-through taxes should not be assigned a
727 revenue lag because they are payable after revenues are collected from customers,
728 stating in the final Order:

729 The Commission agrees with Staff's interpretation as to the
730 EAC/REC and GRT/MUT tax issues. For the EAC/REC tax, the
731 utility shall remit all moneys received as payment to the Illinois
732 Department of Revenue by the 20th day of the month *following the*
733 *month of collection*. Under the GRT/MUT tax, this ordinance
734 requires ComEd to file a monthly tax return to accompany the
735 remittance of such taxes, due by the last day of the month
736 following the month during which such tax is *collected*. Both the
737 statute and ordinance requires ComEd to remit these pass-through
738 taxes after they have been collected from customers. ComEd
739 stated in its briefs that the Company correctly pays these taxes in
740 the month following activity that occurs in a prior "tax liability"
741 month. The Commission concludes that the CWC calculation for
742 GRT/MUT pass-through taxes should reflect zero revenue lag days
743 and 44.21 expense lead days and zero revenue lag days and 35.21
744 expense lead days for EAC/REC pass-through taxes as supported
745 by Staff. [Final Order page 48]

746 The adjustments I have proposed at lines 10 through 12 of AG/AARP
747 Exhibit 1.3, page 2 have the effect of eliminating the revenue lag day values
748 for these pass-through amounts, as previously ordered by the Commission.

749 Additionally, I have revised the expense lead day value for the
750 Energy Assistance Charge because 305 ILCS 20/13 provides that a public

utility engaged in the delivery of electricity shall assess each of its customer accounts a monthly charge and shall remit all moneys received as payment to the Illinois Department of Revenue by the 20th day of the month following the month of collection. These terms yield an expense lead days value of 20 days, plus half of the prior month of 15.2 days, for a total expense lead of 35.2 days

Q. Why have you set to zero the Revenue Lag Day and Expense Lead Day values at line 17 of AG/AARP Exhibit 1.3, page 2?

A. The Company's lead lag study applies revenue and expense lead/lag calculations to about \$77 million of Income Taxes, as if such amounts represent cash transactions. However, in the test year, more than 100 percent of AIC income taxes are "deferred" taxes, largely because of sizable income tax deductions being taken for bonus tax depreciation. At AIC Schedule C-5a, test year recorded income tax expense of approximately \$66 million consists of about \$116 million of deferred income tax expense and about \$50 million of negative current income tax expense. After all of Ameren's proposed ratemaking adjustments and its proposed revenue reduction, adjusted currently payable income tax expense remains substantially negative, as shown in the following table:

774

Test Year Income Tax Expense	Currently Payable	Deferred	Test Year Per Books Tax Expense	AIC Current Income Tax Adjustments	Adjusted Currently Payable
State Income Taxes	(8,870)	21,258	12,388	8,867	(3)
Federal Income Taxes	(39,423)	94,480	55,057	1,995	(37,428)
Investment Credits	<u>(1,245)</u>	=	<u>(1,245)</u>	=	<u>(1,245)</u>
Total Income Taxes	(49,538)	115,738	66,200	10,862	(38,676)

775

Source: AIC Schedules C-5a page 3 and C-1 page 3

776

The breakdown of income tax expenses between the amounts that are

777

deferred versus currently payable is very important in determining CWC,

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because deferred income tax expense represents a non-cash accrual for

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taxes that are expected to become payable in future years, while only the

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“currently payable” income tax expenses are cash costs that are relevant in

781

determining CWC.

782 **Q.**

Why have you assigned zero revenue lag and expense lead values to

783

AIC’s test year income tax expense at AG/AARP Exhibit 1.3, page 2,

784

line 17?

785 **A.**

Because test year adjusted income taxes currently payable are substantially

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negative, it is inappropriate to assign any CWC to this expense. More than

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100% of AIC test year income taxes are actually non-cash deferred income

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taxes, for which there is no current period cash flow that could contribute

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to CWC. It is therefore essential that no lead/lag values be applied to this

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non-cash expense element. This result can be achieved by either setting the

lead/lag values to zero or setting the test year income tax expense amount to zero within the CWC computations.

Q. Was this “setting to zero” approach for income tax expenses employed by ComEd in its formula rate case evidence in Docket No. 11-0721?

A. Yes. ComEd is also deferring all of its income tax liability due to bonus depreciation and other favorable tax deductions it is able to claim. In ComEd Surrebuttal Exhibit 25.1, Mr. Hengtgen revised that utility’s lead/lag study by setting currently payable income taxes at zero so as to eliminate any CWC for ComEd’s non-cash deferred income tax expense recoveries from ratepayers. That same result is necessary in determining AIC’s cash working capital allowance.

Q. After the lead/lag study adjustments you have proposed, should the negative Cash Working Capital amount you have calculated at line 20 in column (I) of AG/AARP Exhibit 1.3, page 2 be included in the Company’s rate base for determination of the inception rates in this Docket No. 12-0001?

A. Not directly. The lead day values and factors from columns (h) through (k) of my Exhibit should be used to determine CWC within the Commission’s rate order, after updating the annual expense and pass-through tax amounts in column (b) at lines 1 through 17 to match the amounts that are finally approved for ratemaking purposes by the Commission. I expect the result of such updating to be negative CWC. A negative CWC result is indicative of the fact that Ameren’s ratepayers, employees, vendors and taxing

authorities, rather than its investors, are supplying the net cash working capital that is required to operate the business. This negative amount should be included in rate base to fully and properly quantify investors' overall net investment in rate base.

V. LATE PAYMENT REVENUE ALLOCATIONS.

Q. What are Late Payment Charge revenues and how have they been treated in the AIU formula rate filing?

A. Late Payment Charges are added to ratepayers' bills when payments have not been received by the due dates of the bills. AIU Electric Service Schedule Ill. C.C No.1, Original Sheet No. 3.018 provides for a "...late payment charge equal to 1.5% per month will be assessed on any amount considered past due," as more fully described in the tariff. In the test year, Ameren recorded as "forfeited discounts" in Account 450 total late payment revenues of \$11.38 million, as shown at Ameren Ex. 2.1, page 28 within App 10. However, the Company applies a "revenue" based allocation factor of 41.89% which results in only \$4.767 million of the total recorded late payment revenues being recognized for ratemaking purposes. This small \$4.767 million value is carried forward as part of the total of \$24.7 million of Other Operating Revenues from line 14 of App 10, for inclusion as a revenue credit to the overall revenue requirement at Ameren Exhibit 2.1, page 1 (Sch. FR A-1) at line 21.

836 **Q. What will happen to the other 58.11% of the AIU late payment revenues that**
837 **the Company seeks to treat as non-jurisdictional for ratemaking purposes in**
838 **its Exhibit 2.1?**

839 A. The balance of late payment charge revenues not being credited to reduce the
840 revenue requirement will be retained by shareholders, because no other regulatory
841 jurisdiction would receive any revenue credits for this other 58.11% share.

842 **Q. Why has Ameren applied a revenue-based allocation factor to the recorded**
843 **late payment charge revenues it earned in 2010?**

844 A. According to the Company's response to AG 4.14, "The reason that Ameren Illinois
845 attributes only 41.89% of such revenues to electric delivery service is because
846 41.89% of revenues from a customer's electric bill that generates the late payment
847 charges is for electric delivery service." This response provides additional
848 arguments for shareholder retention of late payment charge revenues and has been
849 included within AG/AARP Exhibit 1.5 in its entirety. Additional information
850 regarding the Company's proposed allocation of late payment revenues is set forth
851 in the AIU responses to Data Requests AG 1.07, 1.16, 4.13 and AG 6.03, which are
852 also contained within AG/AARP Exhibit 1.5.

853 **Q. Does Ameren provide service in another jurisdiction besides the Illinois**
854 **Commerce Commission?**

855 A. Yes. Wholesale transmission services are regulated by the FERC and AIU submits
856 annual formula rate adjustment applications with the FERC to update its cost-based
857 open access transmission rates based upon current costs and revenues. When
858 allocations are aligned or conformed between the ICC and FERC jurisdictions,
859 Ameren will recover 100% of its costs overall after consideration is given to

expenses, rate base investments and revenue credits that are available to offset such costs. AIU does not provide service in any jurisdictions other than the ICC and the FERC.

Q. Does the Company allocate any portion of its late payment revenues to the FERC jurisdiction for ratemaking purposes?

A. No. The Company admitted in its response to AG 1.07(d) that, “None of the Illinois Forfeited Discount revenues have [been] treated as a revenue credit in determining Ameren’s FERC transmission revenues in the Companies’ most recent transmission rate adjustment proceeding.”²⁶

Q. Has the Commission previously addressed the proper jurisdictional allocation of late payment revenues in any recent rate case?

A. Yes. In Docket No. 10-0467 ComEd had proposed retaining a substantial share of its late payment revenues, through application of a revenue-based allocation factor. In its final Order, the Commission rejected the Company’s proposed changes, stating:

ComEd has classified the \$13.986 million as non-jurisdictional. However, as CUB points out, the only “other jurisdiction” that ComEd is subject to is the FERC. Yet clearly, except for \$2 million, which was accounted for by Mr. Effron, these are not FERC-related charges. Additionally, ComEd is in the business of delivering electricity. In that capacity, to many customers, it provides the electricity to deliver. Therefore, whether the late charges are upon delivery charges or upon the electricity delivered, they are imposed to the delivery service that ComEd provides to the individual customer involved.

To illustrate the fallacy of ComEd’s argument, the Commission points out that a consumer’s total bill has many charges, including such items as those for state and local taxes. The interest charge is imposed on all of these charges. Yet, it cannot be said that state and local taxes are non-jurisdictional. The

²⁶ See AG/AARP Exhibit 1.5; AIU response to AG 1.07.

Commission concludes that ComEd has failed to establish, on an evidentiary basis, that a portion of these charges is not jurisdictional.

On Exceptions, ComEd avers that the conclusions above are inconsistent with other instances in which this Commission has found charges to be jurisdictional. (ComEd Brief on Exceptions at 100-101). However, this situation, unlike the other situations, clearly does not involve non-jurisdictional charges.

The Commission further rejects ComEd's argument that, pursuant to AG/CUB witness Brosch's approach, retail electric suppliers' customers would receive an unfair "advantage," due to the fact that they are subject to a lesser charge to ComEd (but one that will undoubtedly also be charged by retail electric suppliers). There has been no showing here that the system, which creates the potential for great profit (late payment charges) for bundled service customers who are late, versus a lesser profit for ComEd (use of a retail electric suppliers for the supply of electricity, and, therefore, a lesser amount, upon which, ComEd can charge a late payment fee percentage) creates any "advantage" for retail electric suppliers' customers. The only "advantage" is that ComEd receives greater profit from bundled customers. The Commission fails to see how receipt of a greater profit from one group of customers could elevate into discriminatory charges, or, any legally-recognized "advantage." Also, this charge is only imposed upon customers when they do not pay their bills on time. The Commission, therefore, adopts AG/CUB witness Brosch's adjustment on this issue. [Order p. 306]

The situation with regard to Ameren's late payment revenues is nearly identical to that of ComEd, except that Ameren is not crediting any of these revenues to the FERC jurisdiction for ratemaking purposes.

Q. What treatment do you propose with regard to late payment revenues?

A. Late payment revenue should be treated as 100% ICC-jurisdictional and not be subject to any revenue-based allocation factor that would allow Ameren shareholders to retain a portion of such revenues. These amounts are paid entirely by retail ratepayers pursuant to ICC rules and Ameren's Illinois tariff. The

Company has made no showing of that costs were not recovered or any facts that justify shareholder retention of such revenues.

Q. Is Ameren inconsistent in its proposed allocation of late payment charge revenues based upon relative production, transmission and delivery service revenues in Ameren Ex. 2.1, App. 10, given its treatment of other customer provided funds?

A. Yes. Customer Deposits are assessed based upon the relative size of anticipated customer bills and such deposits serve to secure payment for all elements of billed revenues, including recovery of power supply (production), transmission and distribution cost recoveries. However, at Ameren Ex. 2.2, page 51 Workpaper 2, Customer Deposit balances are treated as 100 percent jurisdictional in determining delivery service revenue requirements. This is an appropriate treatment of Customer Deposits and such 100% assignment to retail delivery services should also apply to late payment revenues.

Q. Does the AG/AARP adjustment to Other Revenues appearing in column (d) of your AG/AARP Exhibit 1.3 include a reversal of the AIU proposed jurisdictional allocation of late payment revenues?

A. Yes. A more detailed calculation of the adjustment I proposed is set forth at page 3 of AG/AARP Exhibit 1.3.

VI. REGULATORY ASSET AMORTIZATIONS.

Q. What is required under Section 16-108.5 of the Public Utility Act with regard to the treatment of existing regulatory assets?

953 A. I am advised by counsel that Section 16-108(c)(4)(G) requires that a participating
954 utility's formula shall provide for "recovery of existing regulatory assets over the
955 periods previously authorized by the Commission."

956 **Q. Has AIU included any amortization expenses related to existing regulatory**
957 **assets within its asserted formula rate revenue requirement?**

958 A. Yes. Ameren Ex. 2.1 at page 8, Sch. FR C-1, line 18 includes \$7.131 million of
959 "Regulatory Asset Amortization" within the revenue requirement. This amount is
960 referenced to Ameren Ex. 2.1, page 24 where "App 7" provides a breakdown at
961 lines 33 and 34. The Company's test year regulatory asset amortization amount is
962 comprised of \$352,000 for Severance Cost amortization and \$6,779,000 for
963 Integration Cost amortization.

964 **Q. What was the origin of these two regulatory assets that are being amortized?**

965 A. The Severance Cost amount was incurred and recorded by Ameren in 2009, and
966 was allowed regulatory recovery via amortization in Docket No. 09-0306.
967 Amortization over three years was recorded by AIU, starting in May of 2010 in the
968 monthly amount of \$43,999. Since only eight months of amortization was recorded
969 in 2010, Ameren has included a total of \$352,000 in test year expense for this
970 regulatory asset.

971 Regulatory asset recovery of merger integration costs commenced after
972 Ameren acquired Illinois Power and received regulatory approval in Docket No. 04-
973 0294 for this reorganization and was granted corresponding amortization and
974 recovery of a total of up to \$67 million of merger integration costs over a four year
975 period from 2007 through 2010. In the subsequent Docket No. 09-0306
976 consolidated rate cases, the remaining balance for the integration cost regulatory

asset was recalculated to be amortized over two years. This produced an irregular pattern of monthly integration cost amortization expenses in 2010, with \$1.015 million recorded in each of the first four months of the year and \$0.34 million recorded monthly from May through December of 2010.

I have included as AG/AARP Exhibit 1.6 a complete copy of the AIU responses to Data Requests AG 1.12, AG 4.05, AG 4.06 and AG 4.07 that address these regulatory asset amortization matters.

Q. What are you proposing with regard to regulatory asset amortization expenses?

A. Amortization expense should be adjusted to conform with the amortization periods and amounts most recently approved by the Commission in AIU Docket Nos. 09-0306 consolidated. In those cases, amortization over specified periods produced monthly expense amounts of \$43,999 and \$339,630 for the severance and merger integration regulatory assets, respectively.

Q. Please explain the calculations appearing on AG/AARP Exhibit 1.3 at page 4.

A. Line 1 of this schedule shows the monthly amortization expense previously authorized by the Commission for 2009 Severance Costs (column c) and Merger Integration costs (column d). These amounts are multiplied by 12 at line 2 to derive the equivalent annual amounts last authorized by the Commission. When compared to the Company's proposed annual expense levels (at line 4), the adjustments needed to conform amortization expense to the amortization periods previously authorized by the Commission appear at line 5 and line 6, with the total amount carried forward to AG/AARP Exhibit 1.3, page 1 in column (e).

1000 **Q. Aside from the requirements of the Act, why is it appropriate to restate the test**
1001 **year recorded amortization expenses to match the Commission-authorized**
1002 **recovery periods and amounts?**

1003 A. The AIU rates being set at this time will tend to under-recover severance costs and
1004 over-recover merger integration costs unless my proposed adjustment is made to
1005 restate recorded expenses to ICC-authorized amortization periods and annual
1006 expense levels. Using the rescheduled amortization periods ordered by the
1007 Commission in Docket No. 09-0306 consolidated will also help to ensure that
1008 completion of amortization occurs on the books within a future reconciliation
1009 period, so that ratepayers receive proper reconciliation credit for such expiring
1010 amortizations.

1011

1012 **VII. OPERATING EXPENSE ADJUSTMENTS.**

1013

1014 **A. Lobbying Expense**

1015

1016 **Q. What is the purpose of the adjustment you propose at AG/AARP Exhibit 1.3,**
1017 **page 5?**

1018 A. This adjustment reduces recorded expenses for the portion of Edison Electric
1019 Institute dues in the test year that were incurred for the purpose of influencing
1020 legislation. The quantification of this adjustment was outlined in AIU's response to
1021 AG 4.01, a copy of which has been included in AG/AARP Exhibit 1.7.

1022 **Q. Has Ameren proposed its own adjustment to exclude lobbying expenses**
1023 **incurred in the test year?**

1024 A. Yes. A small adjustment is proposed by Ameren to remove lobbying costs incurred
1025 directly by Company employees, as detailed in Ameren Ex. 2.2, page 103 as part of

Workpaper 7. This small adjustment is posted at Ameren Ex. 2.1, page 23 (App 7) at line 11. The additional EEI dues adjustment I propose is necessary to more completely reclassify AIU's lobbying activities and expenses to below the line accounts to be borne by shareholders rather than ratepayers.

B. Corporate Branding Expenses

Q. Please describe the adjustment appearing at page 6 of AGAARP Exhibit 1.3.

A. In response to Data Request ST 2.07, AIU provided copies of and details regarding advertising, corporate branding and event sponsorship expenses incurred in the test year. The adjustment I propose would remove expenses incurred to examine the Ameren name and corporate logo, including work done by a contractor to transition to the Ameren Illinois name within the Community and Public Relations functions. Line 2 proposes a further exclusion of expenses incurred to provide corporate branded merchandise within an internal store for employees. These expenses are not reasonable or necessary for the provision of utility services and should be excluded in setting rates. Line 6 of this adjustment removes expenses incurred by Ameren for corporate sponsorship of community and sporting events that are discretionary expenses not required for the provision of utility services. AG/AARP Exhibit 1.8 contains a copy of AIU's response to ST 2.07 and Attachment 1 containing a breakdown of expenses including those included in the AG/AARP Adjustment at pages 16 and 19 of Attachment 1.

C. Athletic and Corporate Sponsorship Expenses

Q. What is the purpose of the adjustment appearing at page 8 of AG/AARP Exhibit 1.3?

1049 A. In its response to Staff Data Request ST 2.06, Ameren identified a number of test
1050 year expenditures for tickets, signage and sponsorship costs for various athletic
1051 events. These expenses are not a reasonable and necessary business expense
1052 required to be incurred to provide public utility services and have been disallowed
1053 in the proposed Adjustment. A copy of Ameren's confidential response to ST 2.06
1054 and its Attachment 1 are provided within AG/AARP Exhibit No. 1.8.
1055

1056 **VIII. CONSTRUCTION WORK IN PROGRESS.**
1057

1058 **Q. What is the purpose of the adjustment you proposed at AG/AARP Exhibit 1.3,**
1059 **page 7?**

1060 A. Ameren has included a list of projects that were included in its balance of CWIP not
1061 earning AFUDC as of December 31, 2010. These projects are listed at Ameren Ex.
1062 2.2, page 169 at Workpaper 15, with the total of \$548,683 being proposed for rate
1063 base inclusion. The Company has identified Accounts Payable related to several of
1064 the listed projects, as set forth at lines 3 through 5 of AG/AARP Exhibit 1.3, page 7,
1065 which means that vendors rather than shareholders have funded these CWIP
1066 investments as of year-end. To recognize this non-shareholder funding for CWIP, I
1067 have quantified the adjustment needed to reduce Ameren's asserted rate base for
1068 CWIP not subject to AFUDC that has not been funded by AIC investors.

1069 **Q. How did you determine which of AIC's CWIP projects were funded by**
1070 **Accounts Payable?**

1071 A. In its response to AG 4.16, the Company provided the necessary information to
1072 quantify this adjustment. I have included a copy of this response in AG/AARP
1073 Exhibit 1.9.

1074 **Q. Has the Commission previously concluded that CWIP allowed into rate base**
1075 **should be reduced to account for related Accounts Payable balances?**

1076 A. Yes. In its order in ComEd Docket No. 10-0467, the Commission stated:

1077 ...It appears that there was no attempt on the part of
1078 ComEd to determine what, if any, of these smaller projects
1079 are funded by the lag between the time when they are
1080 booked and when the bills for these items/payment to
1081 employees or contractors are actually paid. As the AG and
1082 CUB point out, many of these items can be temporarily
1083 financed by time. Additionally, the AG asserts that
1084 ComEd's lead/lag study does not include CWIP-related
1085 items and ComEd's evidence provides no specifics
1086 indicating that the AG or Mr. Brosch are wrong in this
1087 regard.

1088 While Ms. Houtsma's testimony in this regard is
1089 vague, the Commission cannot conclude that it is
1090 inadmissible as a matter of law. (*e.g.*, Fraley v. City of
1091 Elgin, 251 Ill. App. 3d 72, 76-77, 621 N.E.2d 276 (2nd Dist.
1092 1993), discussing when factual conclusions are totally
1093 unsupported factually, and therefore may be disregarded, as
1094 a matter of law). \$12.6 million is at issue, and it concerns
1095 many, many, small projects that can be completed quickly.
1096 The Commission also cannot state, within a reasonable
1097 degree of certainty, that all of these projects are vendor-
1098 financed. The Commission appreciates the fact that
1099 accrual-based accounting records record items that will
1100 become due and owing in the future, as opposed to when
1101 the bills for those projects become due and owing. The
1102 Commission also appreciates the fact that there can be a lag
1103 between when work is performed and when the bill for that
1104 work is paid. However, without evidence indicating that
1105 these two lags allow ComEd to pay for its CWIP-related
1106 projects, the Commission cannot state, within a reasonable
1107 degree of certainty, that ComEd's CWIP-related projects
1108 are financed by these two lags.

1109 *However, in ComEd's next rate case, any lead/lag*
1110 *study shall include the effect of accrual accounting on*
1111 *payment for its smaller CWIP-related payments (the*
1112 *payments that are at issue here and that are not accounted*
1113 *for with AFUDC). Failure to do so could result in a*
1114 *determination that ComEd did not meet its burden of proof,*
1115 *or, that ComEd failed to comply with a Commission Order,*
1116 *with all of the penalties that are provided for such failure in*
1117 *the Public Utilities Act.*

1118

1119 Docket No. 10-0467, Order of May 24, 2011 at 30-31 (emphasis added).

1120 **IX. CONCLUSION AND RECOMMENDATION.**

1121

1122 **Q. What is your recommendation regarding the initial revenue requirement to be**
1123 **determined for Ameren in this Docket?**

1124 A. I recommend that AIC's delivery service revenue requirement be found to be no
1125 larger than the amount shown in AG/AARP Exhibit 1.3, at page 1, line 25 in
1126 column (k). This amount should be further modified for any Commission-approved
1127 ratemaking adjustments proposed by the Staff and other parties, that are not
1128 addressed in my or Mr. Effron's Direct Testimony.

1129 **Q. Does AG/AARP Exhibit 1.3 also include the impact of adjustments being**
1130 **proposed by Mr. Effron?**

1131 A. Yes. Page 1, column (j) of AG/AARP Exhibit 1.3 reflects the overall adjustment to
1132 rate base being supported by Mr. Effron.

1133 **Q. What do you recommend regarding the Company's proposed formula rate**
1134 **template set forth at Ameren Exhibit 2.2?**

1135 A. The AIU formula rate template should be modified as necessary to comport with the
1136 ratemaking decisions reflected in the Commission's Order in this Docket.
1137 Corresponding changes to proposed Rate MAP-P should also be submitted in an
1138 AIU compliance filing, subject to review by Staff and other parties, prior to the new
1139 formula rate tariff being made effective.

1140 **Q. Does this conclude your testimony at this time?**

1141 A. Yes.